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Before the
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Annual Compliance Report, 2013 Docket No. ACR2013

PUBLIC REPRESENTATIVE COMMENTS
(January 31, 2014)

Respectfully submitted,

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TABLE OF CONTENTS

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Pursuant to the Commission's Notice in this proceeding,[1] the Public Representative hereby comments on the Postal Service's 2013 Annual Compliance Report (2013 ACR) filed for fiscal year 2013 as prescribed by the Postal Accountability and Enforcement Act (PAEA). 39 U.S.C. § 3652.[2]

The Postal Service's 2013 ACR is "to demonstrate that all products during the year complied with all applicable requirements of [title 39]." 39 U.S.C. § 3652(a)(1). These Comments address matters relating to the Postal Service's (1) financial condition, (2) service performance (3) customer access (4) market dominant products (4) worksharing and (4) competitive products.[3]

The Public Representative has reviewed the Postal Service's FY2013 Annual Compliance Report together with previous Commission Annual Compliance Determinations (ACDs) and the Commission's directives and recommendations for Postal Service action in those proceedings. Since the passage of the PAEA, the

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[1] Notice of Postal Service's Filing of Annual Compliance Report and Request for Public Comments, December 30, 2013.

[2] United States Postal Service FY 2013 Annual Compliance Report (2013 ACR), December 27, 2013.

[3] Comments on the Postal Service's strategic initiatives and performance plans required by 39 U.S.C. § 2803 and § 2804 and included in the ACR are deferred to no later than March 10, 2014. Reply comments on those matters are due no later than March 20, 2014. Notice Regarding the Postal Service's FY 2013 Performance Report and FY 2014 Performance Plan, January 17, 2014.

Commission's annual analysis of the Annual Compliance Reports has matured and stabilized with primary focus on the financial difficulties of the Postal Service, and on review of service performance and customer access, market dominant product cost coverages, worksharing passthroughs, contribution from competitive products, and nonpostal services. Service performance reports and plans are also reviewed annually.

Overall, with respect to the 2013 ACR, the Public Representative finds that prior deficiencies in the annual compliance report generally are being satisfactorily ameliorated or eliminated. During FY2013, the Postal Service moved in the right direction by reducing its program costs and services and adjusting rates and its rate designs to improve contribution shortfalls that have been necessitated by declining mail volumes, the crushing burden of payments to the Retirement Health Benefits Fund (RHBF), its $15 billion debt ceiling, and the price cap limitation in the PAEA.

These Comments discuss areas in need of improvement, both in Postal Service methodology, operations and rates and in presentation of the ACR. There is also some focus on Postal Service methodology and rates for certain competitive international products. The Public Representative also encourages the Commission to order the Postal Service to cancel one of its competitive contracts that failed to cover attributable costs.

I. INTRODUCTION

In each review of a Postal Service ACR, the Commission is charged with determining: (1) whether any rates or fees in effect during the preceding year were not in compliance with chapter 36 of title 39 and its accompanying regulations, (2) whether any service standards in effect during the preceding year were not met. 39 U.S.C. § 3653(b), and (3) may recommend actions to the Postal Service for the protection or promotion of the public policy objectives of title 39. 39 U.S.C. § 3653(d). In addition, the Commission is to evaluate whether the Postal Service has met the goals related to performance and planning established pursuant to sections 2803 and 2804 of title 39. Comments on the latter matters have been deferred as noted above.

II. FINANCIAL REVIEW

A. Introduction

The provisions of the PAEA provide for a modern system of rate regulation implemented by the Commission with an objective to, among other things, "assure adequate revenues, including retained earnings, to maintain financial stability." 39 U.S.C. § 3622(b)(5). The Postal Service is required pursuant to 39 U.S.C. § 3652 to file with the Commission an Annual Compliance Report to demonstrate the Postal Service's products during the year complied with all requirements of title 39. The Postal Service is also required by 39 U.S.C. § 3652(g) to file a comprehensive statement detailed under section 2401(e) to include total expenditures and other information to inform fully Congress on postal operations.[4]

If the Commission finds pursuant to review under 39 U.S.C. § 3653, that the Postal Service products failed to comply with all applicable requirements of title 39 during the year under review, the Commission has authority to exercise its discretion to remedy the noncompliance through the broad provisions of 39 U.S.C. § 3662. Whether the Postal Service's products provided adequate revenues to maintain financial stability in accord with the provisions of title 39 is one factor that must be weighed by the Commission in this proceeding.

A determination of whether the products complied with title 39 sufficiently to, among other factors, maintain financial stability, should include a comprehensive review of the Postal Service's rates and products and the income generated by the totality of

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[4] The FY2013 Comprehensive Statement on Postal Operations was filed in this docket as part of the ACR as a portion of library reference USPS-FY13-17 at 45-74.

those products for the year under review. For this, the information supporting net income reports are necessary. One must look beyond the ACR for this information. The Integrated Financial Plan (FY2014 IFP) filed with the Commission on November 25, 2013 and the Form 10-K file November 15, 2013 contain that financial information.

Fiscal year 2013 was a year of financial improvement in operations for the Postal Service after several years of increasing deficits from operations. If the Postal Service's obligations to pay into the RHBF are taken into account, the Postal Service's loss in FY 2013 was $5.0.[5]

A review of the Postal Service's financial results, absent its retirement fund obligations, provides a picture of the Postal Service's financial results from operations. Although the inability to make any payments into the RHBF continues to add over $5 billion per year to the liability side of the balance sheet, the financial results from operations can best be viewed as if those payments were not required. Similarly, for purposes of viewing results from operations, the Postal Service has excluded for FY2013 the impact of Workers' Compensation discount rate changes and actuarial reevaluations of stamps in the hands of the public that therefore resulted in its computed $1.0 billion operating loss.[6] With these adjustments, the Postal Service's FY 2013 operating losses were cut by much more than half, to $1.0 billion, continuing to fall from losses on operations of $2.7 billion and $2.4 billion in FY2011 and FY2012, respectively.[7]

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[5] FY 2014 IFP at 1.

[6] .*Id*.

[7] USPS-FY13-17 at 39.

B. Sufficiency of Financial Reports

Although the financial stability of the Postal Service is a factor the Commission must consider when reviewing the Postal Service's compliance with title 39, the 2013 ACR contains virtually no financial information.

The 56 page text of the Postal Service's ACR does not mention its annual income (or loss) and the library references offered in this proceeding do not include detailed information on income or loss. The Postal Service's FY2013 Annual Report to Congress contains very limited financial information.[8] That library reference includes the Postal Service's FY2013 Comprehensive Statement on Postal Operations required to be submitted with the ACR by 39 U.S.C. § 3652. Oddly, the Postal Service's Road Map library reference in the ACR specifically states that the Postal Service does not rely upon the information in the Comprehensive Statement on Postal Operations.[9] Only the FY2013 Annual Performance Report cites to an actual operating loss in FY13 of $1.0 billion and a target loss of $2.0 billion in FY13. *Id*. at 39.[10] There is no balance sheet or income statement included in the ACR.[11]

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[8] Library Reference USPS-FY13-17.

[9] The Road Map states, "Since this item is provided as general background information, it is not directly relied upon by the Postal Service in this filing." USPS-FY13-9, Roadmap Document, to FY 2013 Annual Compliance Report at 22.

[10] Excluding Workers' Compensation rate adjustments and USPS Retiree Health Benefit Fund (RHBF obligations. FY2013 Annual Performance Report and FY2014 Performance Plan at 39. "Financial results" is listed as one of four goals of the Postal Service in that report. The table in the Comprehensive Statement lists four categories of goals: Service (% on-time), Customer experience, Financial results and Workplace environment together with the measure for each goal. In the case of financial results, the measure are Operating income (loss) and Deliveries per hour. *Id.* Inasmuch as the cited goals are only categories, the Postal Service apparently assumes the goal is an increase in the measured amount for each goal over a period of time.

[11] Detailed financial information is contained only in the Annual Report, Form 10-K filed with the Commission pursuant to 39 C.F.R.3050.40 on November 15, 2013.

C. Improvements in Working Capital

Although earnings in FY 2013 show improvement year over year, during FY 2013, the Postal Service continued its downward financial slide due to price cap restrictions and the RHBF payments that will continue until Congress grants legislative relief. In FY 2012, without considering the burden of RHBF and Worker's Compensation Expenses, the loss was $2.4 billion while the FY 2013 plan was to improve that slightly with a $2 billion loss.[12]

During FY 2013 the Postal Service's cash position finally showed some signs of improvement even though losses continued and the Postal Service has reached its borrowing limit from the U.S. Treasury of $15 billion. The Postal Service's cash at the beginning of FY 2013 was $2.1 billion.[13] The Postal Service estimated it would end FY 2013 with only $0.8 billion in cash, a dangerously low level of liquidity and equivalent to four days of cash operating costs. FY2013 IFP at 6. The Postal Service actually ended FY 2013 with $2.3 billion of unrestricted cash, better than predicted. FY2014 IFP at 7. With the revenue from recently approved rate increases for the cost of living increase and exigent circumstances, effective January 26, 2014, the Postal Service predicts a further improvement in its working cash with an unrestricted cash position at the end of FY 2014 of $4.5 billion. *Id.* at 8.

D. Capital Commitments Increased in FY2013 but Capital Cash Outlays Fell

Capital commitments of the Postal Service target projects with high investment returns. The Postal Service is continuing its efforts to conserve cash. The Postal Service's FY2014 IFP discusses its capital commitments. Actual cash commitments for facilities, equipment, and infrastructure and

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[12] Recent losses have been (in billions): FY 2010--$5.505; FY 2009--$3.794; FY 2008--$2.806; FY 2007--$5.142. Section 701 Report, Analysis of the Postal Accountability and Enhancement Act of 2006, Postal Regulatory Commission, September 22, 2011 at 22.

[13] FY2014 IFP at 6; Annual Report to Congress 2012 at 20. The Annual Report indicates end of year cash of $2.3 billion, but the IFP notes $0.2 billion is restricted; thus the two reports are consistent.

support increased significantly in FY2013 to $0.8 billion, up from $0.5 billion in FY2012, but significantly below the 5 year average (2007-2011) of $1.4 billion. For FY2014, the Postal Service plans to increase capital commitments by 50 percent to $1.2 billion. Facilities commitments will remain constant at $0.4 billion but capital commitments for equipment and infrastructure and support will double to $0.4 billion. FY2014 IFP at 6.

Actual capital cash outlays for facilities, equipment, and infrastructure and support for FY 2013 totaled $0.7 billion, down from $0.8 billion in FY2012 and also far below the 5 year average (2007-20011) for cash outlays of $1.8 billion. For FY2014, although maintaining its efforts to conserve cash, the Postal Service also plans a significant increase in capital cash outlays from $0.7 billion to $1.0 billion. Capital cash outlays for facilities will increase from $0.3 billion to $0.4 billion. Outlays for equipment and infrastructure and support will increase by 50 percent from $0.2 billion to $0.3 billion. *Id*.

The FY2014 IFP Report states that the Postal Service continues to have insufficient liquidity to make needed investments in infrastructure. *Id*. at 9. A report by the Postal Service's Office of Inspector General (OIG) during FY2013 echoes this concern. The OIG found budget constraints have affected its ability to fund repairs, alterations, and capital improvements, almost 30 percent below the industry average for facility repairs.[14] Delayed repairs escalate the ultimate repair cost. The impact of unfunded repairs in FY2011 and FY2012 could reach $1.4 billion. *Id*.

E. Service Curtailment Plan Due to Cash Shortages Is Not Now Required

The Public Representative's Comments on the 2012 ACR expressed concern that low cash levels coupled with the possibility of small changes in cash requirements due to unforeseen circumstances could quickly lead to an

[14] Office of the Inspector General, United States Postal Service, Spending Trends for Maintaining Postal Service Facilities, Audit Report, November 27, 2013 at 1.

inability to met financial obligations, not only from a financial standpoint, but from the standpoint of potential service disruptions and the impact on mailers and its ability to provide effective and nondiscriminatory regular postal services.

Consequently, the Public Representative's Comments on the FY 2012 ACR proposed that the Commission should request a description of the Postal Service's priorities and plans for providing service across the Nation and across classes in the event cash shortages require services to be reduced.

In its Integrated Financial Plan for FY 2014, the Postal Service provided a chart demonstrating its improved cash situation during FY2013 and estimates for FY2014.[15] The available unrestricted cash in mid-October 2012, just after the beginning of FY2013, was only $1 billion, representing 4 days of cash requirements. The cash position improved throughout FY2013, and just after the end of 2013, mid-October 2013, cash was about $1.8 billion, representing 6 days of cash requirements.[16] Happily, it does not appear that there were any unexpected or unplanned reductions in operations for services directly due to cash shortages during FY2013. In FY2014, the Postal Service's cash position is expected to improve markedly from the $1.8 billion available at the beginning of this fiscal year to almost $4 billion, or 14 days of cash requirements by the end of the fiscal year in September 2014. FY2014 IFP at 8.

This improved cash position is likely to continue, at least for the years of increased revenue due to the exigent rate increase. Therefore, in the absence of potential need this year, the Public Representative does not see a need at this time to request again the Postal Service's priorities and plans for providing service across the Nation and across classes in the event cash shortages require services to be reduced.

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[15] FY2014 IFP, Chart of Liquidity Days of Operating Cash Available at 8.

[16] At the beginning of October 2013, the cash was available for 9 days of operations. USPS-FY13-17 at 41.

III. SERVICE PERFORMANCE

The Postal Service presents its service performance for each market dominant product in the Annual Report on Service Performance for Market Dominant Products. USPS-FY13-29.

A. First Class Mail

Table III-1 shows several Postal Service measures of annual service performance for First Class Mail products. Table 1 shows that the Single-Piece and Presort First-Class letters and postcards exceeded its service targets in FY 2013 except Three-To-Five-Day Single-Piece letters/cards. The Postal Service explains that inclement weather during the first two quarters is responsible for the 3-5 day mail missing its standard. USPS-FY-13-29, Service Performance ACR FY13.pdf (Service Performance) at 8. This seems to be a plausible explanation. However, even if the percentage of First-Class Single Piece Letters and Cards (SPLC) with 3-5 day delivery were to increase by 3 percent, SPLC would barely exceed its target delivery percentage. Table III also shows that Flats, Parcels, and Combined International all fell well below their service targets. With the exception of Presort Letters and Cards, all categories of First-Class Mail require greater improvement in order to meet their on-time delivery percentage targets with a high degree of certainty.

Table III-1
Service Performance: First Class Mail

	Target %	% On-Time	Beat Target?	How much? (%)
Single-Piece				
Overnight	96.70	96.80	Yes	0.1%
Two-Day	95.10	96.00	Yes	0.9%
Three-To-Five-Day	95.00	92.50	No	-2.5%
Presort				
Overnight	96.70	97.30	Yes	0.6%
Two-Day	95.10	97.20	Yes	2.1%
Three-To-Five-Day	95.00	95.40	Yes	0.4%
Flats				
Overnight	96.70	86.57	No	-10.1%

Two-Day	95.10	84.39	No	-10.7%
Three-To-Five-Day	95.00	77.58	No	-17.4%
Parcels				
Overnight	96.70	89.80	No	-6.9%
Two-Day	95.10	89.10	No	-6.0%
Three-To-Five-Day	95.00	88.80	No	-6.2%
Outbound Single-Piece				
Combined	94.00	88.90	No	-5.1%
Inbound Single-Piece				
Combined	94.00	88.00	No	-6.0%

Source: USPS-FY13-29, FY13 ACR First-Class Mail.xls, "FCM On-Time Performance."

B. Standard Mail

The data for on-time delivery of Standard Mail are mixed. The Postal Service reports that only High Density and Saturation Letters met their target delivery window. All other mail categories are substantially below their target delivery windows. The Postal Service explains that although Standard Mail did not meet target on-time delivery percentages, "work-in-process diagnostics for Standard Mail, [resulted in]…continued steady improvements in Standard Mail service performance. *Id.* at 12.

The Public Representative examined the quarterly on-time delivery data provided by the Postal Service, and reproduces the results in Table 2. It shows the percentage change in on-time delivery by quarter. Most of the improvement occurs in the second quarter of the year, and then drops off during the third and fourth quarters. The fact that the greatest improvement in on-time delivery occurs in the second quarter, and then rapidly drops in the following quarter, suggests a seasonal pattern is at work, and that the diagnostic tools to which the Postal Service refers might be applied more specifically toward improving fourth quarter deliveries.

Table III-2
Quarterly Percentage Change in On-Time Delivery for Standard Mail

	Percent on Time		
	Q1-Q2	Q2-Q3	Q3-Q4
High Density and Saturation Letters	4.8	1.5	0.0
Carrier Route	12.5	3.6	-2.0
Letters	3.1	3.6	0.5
Flats	3.7	4.5	0.3

Parcels	-0.6		
Mixed Product Standard Letters	2.3	6.1	0.4
Mixed Product Standard Flats	9.3	1.3	2.5

Source: USPS-FY13-29, FY13 ACR Standard Mail.xls, "Aggregation."

C. Periodicals

Periodicals also had a mixed performance record this year with on-time delivery improving 13 percentage points over last year. *Id*, at 15. Nevertheless, on-time delivery of Periodicals remained 10 percent below performance goals. The Postal Service states that the percent of Periodicals Mail delivered on-time "consistently improved Periodicals service performance over all quarters." *Id*. It attributes this improvement to its use of automation and the same type of diagnostics used to improve Standard Mail delivery performance. Service Performance at 15. A close look at the data shows that nearly all of the improvement occurred during the second quarter of the year and declined in the third quarter, as shown in Table III-3.

Table III-3
Quarterly Percentage Change in On-Time Delivery of Periodicals

	Percent on Time		
	Q1-Q2	Q2-Q3	Q3-Q4
Periodicals Percent On-Time	83.2	82.7	83.1
Percentage Change in On-Time Delivery	3.8	-0.6	00.4

Source: USPS-FY13-29, FY13 ACR Periodicals.xls, "Aggregation."

This appears to be the same pattern observed for Standard Mail. The Public Representative questions whether the "continuous use of diagnostic tools" by the Postal Service is responsible for improving its on-time delivery. The Commission should have the Postal Service explain why continuous use of the same diagnostic tools every quarter does not produce quarterly improvements in on-time delivery of either Standard Mail or Periodical Mail.

D. Package Services

Packages Services consists of 5 products. The Postal Service either met or approached its FY 2013 service performance target of 90 percent for Bound Printed Matter Parcels, Media Mail/Library Mail, and Inbound Surface Parcel Post (at UPU rates). *Id*. at 20. The performance score for Bound Printed Matter Flats of 62 percent fell substantially short of its 90 percent target, although it improved by 8 percentage points compared to last year.

Once again, the Postal Service attributes its use of diagnostic tools, made possible by increased adoption of Full Service Intelligent Mail, to account for improvement in on-time delivery. *Id.* at 20. Viewing the percentage change in on-time delivery by quarter in Table III-4 does not support the claim that use of diagnostic tools (whether or not related to increased adoption of Full Service IMB) makes continual improvement in delivery possible.

Table III-4
Quarterly Percentage Change in On-Time Delivery for Package Services

	Percent on Time		
	Q1-Q2	Q2-Q3	Q3-Q4
Single-Piece Parcel Post	-1.7	No data	No data
Bound Printed Matter Flats	-0.5	6.2	9.1
Bound Printed Matter Parcels	2.2	0.6	-0.5
Media Mail/Library Mail	2.4	2.1	-1.7
Inbound Surface Parcel Post (at UPU rates)	3.5	1.2	-1.9
Single-Piece Parcel Post (at UPU rates)	-1.7	No data	No data

Source: USPS-FY13-29, FY13 ACR Package Services.xls, “Aggregation.”

Only Bound Printed Matter Flats shows a continual, quarterly, increase in on-time delivery. The other package services with more than one quarter of data show the largest increase in on-time delivery to be the quarter after the holiday season, followed by continual, quarterly reductions in on-time delivery gains during the third quarter and reversals of delivery gains in the fourth quarter.

E. Special Services

The Postal Service states that "[a]ll Special Services achieved the established service targets at the reporting level required in this report. *Id.* at 24. Table III-5 shows that the Postal Service has also improved Special Services on-time delivery an average of slightly more than 2 percent since FY 2012. Table III-5 shows that these 2 services saw a decline of on-time delivery by approximately 2 percentage points in FY 2013 compared to FY 2012. The Postal Service should be commended for improving on-time delivery for most Special Services. The Postal Service should analyze the reasons Ancillary Services and PO Box Service has declined and take steps to improve their on-time delivery.

Table III-5
Special Service On-time Delivery Analysis

	FY 2012	FY 2013	Percentage Change
	% On Time	% On Time	FY13 - FY12
Ancillary Services	93.4	91.4	-2.0
International Ancillary Services	99.6	99.3	-0.3
Address List Services	83.3	100.0	16.7
Confirm®	98.8	99.7	0.9
Money Orders	99.2	99.2	0.0
Post Office™ Box Service	92.6	90.9	-1.7
Stamp Fulfillment Services	96.7	99.5	2.8
Average	94.8	97.1	2.3

Source: USPS-FY13-29, FY13 ACR Special Services.xls, "SS On-Time Performance."
USPS-FY12-29, FY12 ACR Special Services.xls, "SS On-Time Performance."

IV. CUSTOMER ACCESS

A. Introduction

Pursuant to Section 39 C.F.R. 3055.91, the Postal Service is required to provide data on customer access to postal services that includes the number of post offices, collection boxes, delivery points, and wait time in line for retail service in its Annual Compliance Report. The Postal Service has complied with this requirement, and provided data that show, when measured as a district level average, customers received good quality access. However, more disaggregated data could show areas where customer access may need improvement. The Postal Service should report on customer access at more disaggregated levels in future Annual Compliance Reports.

B. Postal Offices

Table IV-1 shows the number of various types of postal offices from FY 2009 to FY 2013.

Table IV-1
Postal Offices FY 2009 to FY 2013

							% Change
Post Offices, stations, and branches	**2013**	**2012**	**2011**	**2010**	**2009**	**Change**	**FY09-FY13**
Total Postal-managed	**31,702**	**31,857**	**32,146**	**32,528**	**32,662**	**-960**	**-2.9%**
Contract Postal Units	**2,718**	**2,792**	**2,904**	**2,931**	**3,037**	**-319**	**-10.5%**
Village Post Offices	**385**	**47**	**0**	**0**	**0**	**385**	
Community Post Offices	**629**	**673**	**706**	**763**	**797**	**-168**	**-21.1%**
Total offices, stations, and branches	**35,434**	**35,369**	**35,756**	**36,222**	**36,496**	**-1,062**	**-2.9%**

Source: http://about.usps.com/publications/annual-report-comprehensive-statement-2013/annualreport2013_034.htm, Viewed 1/27/2014.

Data in Table IV-1 are national numbers. The decline of access to postal units by relevant demographic characteristics, such as whether the area served is rural, low-income, elderly, and has ready to public transportation is not available. It is possible that at-risk demographic groups could be experiencing some additional hardship as a result of the decline in retail access to postal offices.

Contract Postal Units (CPUs), and especially Community Post Offices (CPOs), are not very stable organizational structures. As the data provided by the Postal Service shows,[17] over 13 percent of CPU and CPO that existed at the beginning of FY 2013 were closed during the year. The number of newly opened CPUs and CPOs was less than half the number of those closed. The resulting overall decline in the number of CPOs and CPUs in FY 2013 continues the trend observed over past years.

[17] Response of the United States Postal Service to Questions 4 of Chairman's Information Request No 1, January 15, 2014, file ChIR.1.Q.4.FY13.CPU-CPO.xlsx.

The Postal Service began opening “Village Post Offices” (VPO) in 2012. VPOs are located within existing communities, in locations such as convenience stores, local businesses and libraries, and operated by the management of those locations. VPOs offer products and services most used by customers -- including PO Boxes, Forever stamps, pre-paid Priority Mail Flat Rate envelopes and mail collection boxes. VPOs also often have longer hours than regular Post Offices. The Postal Service states that it opened 338 VPOs in FY 2013 for a total of 385 by the end of FY 2013. 2013 ACR at 43. Community Post Offices-managed retail outlets-have had the largest absolute decline, while other postal service outlets have declined by 1,477 units, approximately 4 percent since 2009. Village Post Offices have added to the number of post office facilities, but have not compensated for the overall decline in retail access.

Finally, VPOs do not fully replace a postal-managed post office. People still need to travel to an office other than a VPO to take advantage of the full array of retail postal services. Moreover, the Postal Service does not discuss here, or in its 2013 ACR what types of problems customers experience at VPOs and whether or not the VPO is able or authorized to resolve such problems. For example, if a mail piece is returned without explanation, can a VPO owner determine the reason for the return from the closest Post Office? Is the VPO authorized to correct such a problem without the customer having to travel to the nearest Post Office? The Post Office should report on such problems and the resolution for problems such as these. It should also consider doing a separate survey of the customer experience at VPOs.

C. Collection Points

Collection points permit customers to drop-off single-piece First-Class Mail into collection boxes in residential neighborhoods or in business districts, lobby drops inside Post Offices, and drops into blue boxes outside Post Offices.[18]

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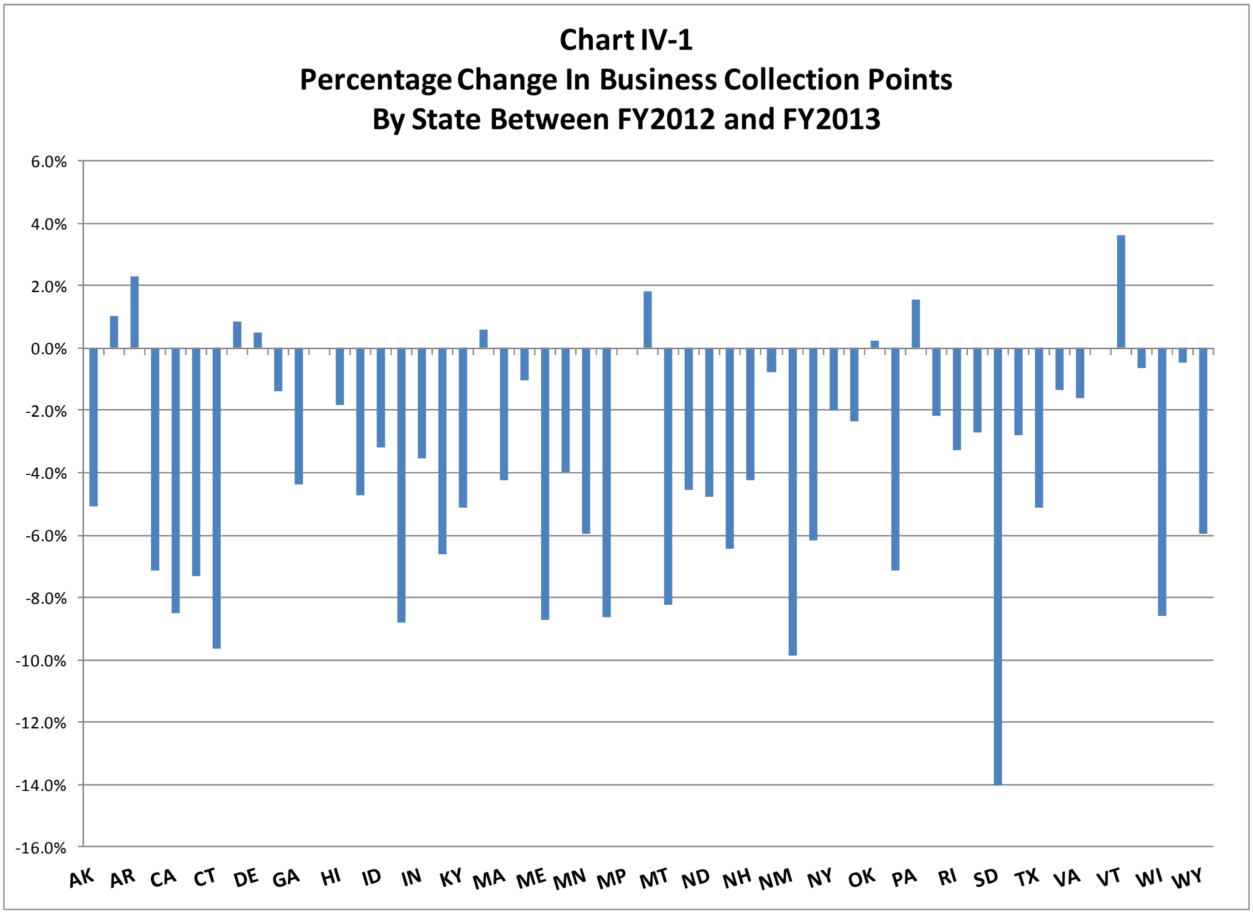
[18] These are the type of Post Offices most likely to be used by residential customers. Other collection points include “Firm,” “Airport,” and “Other.” *See* USPS-FY13-33.

The Postal Service has provided data on the total number of collection boxes for each of the six postal districts for the beginning and end of Fiscal Year 2013. The data show that during FY 2013 collection points were reduced by 4,380, approximately 2.7 percent. USPS-FY13-33-Access, CollectionBoxesFY2013.xls.

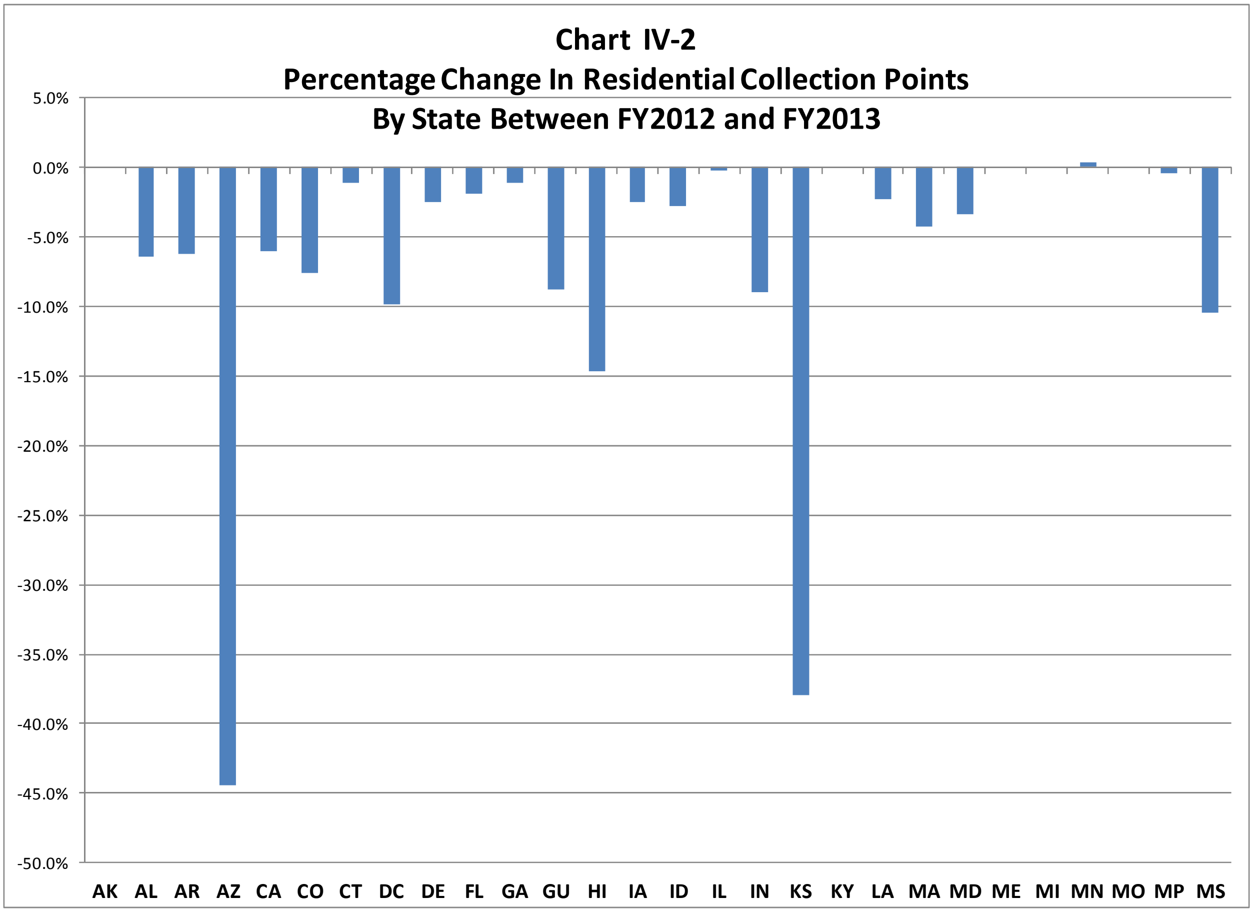
The Commission asked for and received more disaggregated data on collection boxes by 3-digit ZIP Code, Location of the Collection Box, State, and other variables. CHIR No. 1, question 3. The Public Representative has used this data to compare the percentage change of Postal Service collection points in residential and business areas, post office lobbies and outside post offices, by State between the end of FY2012 and FY2013. Between FY 2012 and FY 2013, residential collection points declined by 1,412 -- a 3.4 percent decline. Over the same period, business collection points declined by 3,504 unique points, for a 4.3 percent decline.[19]

State-level disaggregation shows that reductions between FY 2012 and FY 2013 vary substantially by state. Chart IV-1 shows the variation in the percentage change of business collection points by state. Chart IV-2 shows the percentage decline in residential collection points by state, and Chart IV-3 shows the dispersion of the percentage decline in all collection points by state. It is reasonable to presume that states with the largest percentage reductions in residential delivery points will most impact the elderly, medically fragile, and the disabled.

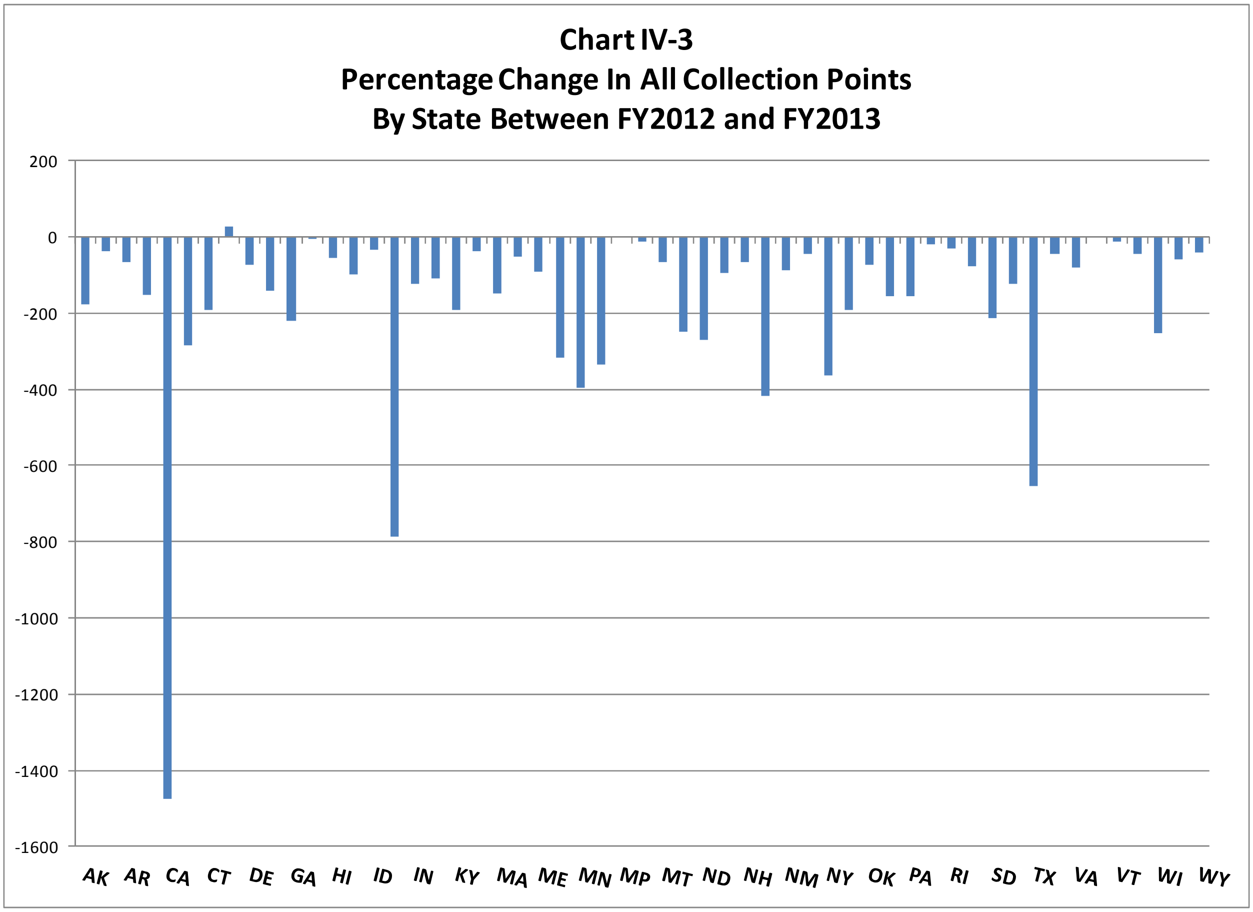
[19] Most collection points have more than one collection receptacle. The Public Representative filtered the data obtained from the Commission's Information Request last year and this year to contain only unique receptacle numbers.



Source: USPS-FY13-43, ChIR1.Q6(CPMS)(1 & 2).xlsx



Source: USPS-FY13-43, ChIR1.Q6(CPMS)(1 & 2).xlsx



Source: USPS-FY13-43, ChIR1.Q6(CPMS)(1 & 2).xlsx

D. Delivery Points

The Postal Service reports that the number of delivery points modestly increased from the beginning of FY 2013 to the end of FY 2013. Table IV-2 shows the absolute and percentage change in types of delivery points during FY 2013.

Table IV-2
Absolute and Percentage Change in Types of Delivery Points

Type of Delivery Point	Annual Change	Percentage Change
Active Residential Curbline	468,930	0.9%
Active Residential Ndcbu	376,974	2.3%
Active Residential Central	190,919	0.9%
Active Residential Other	-59,263	-0.2%
Active Business Curb	16,696	1.2%
Active Business Ndcbu	42,729	4.3%
Active Business Central	10,600	1.7%
Active Business Other	-20,924	-0.4%

Source: USPS-FY13-33.Access, DeliveryPointsFY2013.xls

During, FY2013, active residential delivery points increased by nearly 1 million--approximately 0.8 percent and active business delivery points increased by approximately 49,000 -- approximately 0.6 percent. Total delivery points increased by a little over 1 million points -- approximately 0.8 percent. The largest growth in the type of delivery points for both residential and business was in curbline boxes and neighborhood delivery collection box units (NDCBU). The greatest reductions in residential and business delivery points came from “other” collection points, which the Public Representative presumes is door delivery. This change represents a move to more efficient delivery from home delivery to curbline boxes and NDCBUs. The Public Representative supports the move from door to curbline and NDCBU delivery points when cost effective.

E. Wait Time in Line

The Postal Service reports that “[a]verage wait time in line improved at the national level from 2 minutes 34 seconds in FY 2012 to 2 minutes 29 seconds in FY 2013. Average wait time in line also improved in six of the seven Areas from FY 2012 to FY 2013. FY 2013 ACR at 44. Table IV-3 shows the average wait time by region.

Table IV-3
Average Wait Time in Line by Region

	Minutes & Seconds		Seconds
Area	Retail Wait Time	National Average	
Capital Metro	2:19	2:29	-10.0
Eastern	2:16	2:29	-13.0
Great Lakes	2:00	2:29	-29.0
Northeast	2:21	2:29	-8.0
PACIFIC	3:19	2:29	50.0
Southern	2:22	2:29	-7.0
WESTERN	2:48	2:29	19.0

Source: USPS-FY13-33.Access, WaitTimeInLineFY2013.xlsx, “Area Avg Wait.”

The Pacific and Western Regions had greater than average wait time in line, while the other regions had less than average wait time in line. The Pacific region’s wait time in line was 50 seconds greater than average. While this is not a difference that matters at this level of aggregation, it could indicate a concern for certain offices and/or days of the week in the Pacific region. The Postal Service should look deeper to determine whether this is the case.

V. MARKET DOMINANT PRODUCTS

One important aspect of the improvement in Postal Service operations lies in improved rate designs that resulted in more favorable cost coverages in FY2013. In FY2012, the Commission criticized the Postal Service for the losses from nine market dominant products that failed to generate revenues sufficient to cover attributable costs totaling $1.473 billion. 2012 ACD, Letter from the Chairman at 1, also see 8, and 78. Overall, in FY2013 the Postal Service’s cost coverages for those nine products improved significantly although the cost coverages for three of the products fell slightly,[20] and one for Standard Mail Parcels fell significantly due to product rearrangement. More importantly, the actual dollar shortfall in coverages was

[20] First-Class Parcels and Inbound S-P Mail Intern-l and Package Services Media/Library Mail fell slightly. Table V-1.

significantly reduced as all but one of the nine products reduced the dollar impact of the cost coverage shortfalls. Thus, the total losses in FY2013 for the nine market dominant products below 100 percent cost coverage was reduced by $330 million or about 25 percent to $1.14 billion. The details of these improvements are shown in Table V-1 and discussed below. In FY 2014, as projected in R2013-11, the cost coverage shortfalls would decline to $607.389 million.

Table V-1
Market Dominant Products with
Cost Coverage Below 100 percent in FY 2012-2013

	2012 ACD[1]		2013 ACR[2]		R2013-11[3]	
Product	**Cost Coverage**	**Loss ($ Millions)**	**Cost Coverage**	**Loss ($ Millions)**	**Cost Coverage**	**Loss ($ Millions)**
1st Class						
Parcels	98.5%	9.648	97.22%	16.607	121.26%	N/A
Inbound S-P Mail Int-l	73.1%	92.794	65.58%	78.464		
Periodicals						
Within County	70.5%	28.129	75.18%	21.590	78.84%	17.566
Outside County	72.2%	641.987	75.82%	505.925	80.74%	382.263
Standard Mail						
Flats	80.9%	527.940	84.88%	380.121	92.22%	188.068
Parcels[4]	85.5%	48.959	64.29%	39.157	97.51%	1.821
Package Services						
[Single-Piece] Parcel Post	92.2%	65.921	96.05%	13.054	109.04%	N/A
Media and Library Mail	85.3%	55.524	84.23%	58.715	94.31%	17.671
Special Services						
Stamp Fulfillment Services	59.25%	2.268	82.99%	0.861		
Total:		**1,473.170**		**1,114.494**		**607.389**

[1] ACD 2012, Appendix D Table D-1 at 206 and Table VII at 136.

[2] ACR 2013 at. 10, 17, 31, 34 and 37.

[3] Projected FY2014 'After Rate'. *See* R2013-11, Statement of Stephen Nickerson (Revised on 11/22/13), Attachment 25.

[4] In 2012 the market dominant product Standard Mail Not Flat-Machinables and Parcels was renamed Standard Parcels and was divided into two categories. One of those two categories was moved to the competitive product list on January 22, 2012. *See* ACD 2012 at 18.

These coverages should improve further and significantly in FY2014 due to the annual price cap rate adjustment effective January 26, 2014 and the larger exigent rate increase effective the same date.

A. First-Class Mail Cost Coverage

In FY 2013, all First-Class Mail products covered their attributable cost, except Parcels and Inbound Single-Piece First-Class Mail International.[21] Total First Class Mail cost coverage continued to increase, but at a faster pace than in FY 2012. In FY 2013, First-Class Mail cost coverage increased by 8.9 percent (from 202.9 percent to 211.8 percent), while in FY 2012 it increased by 3.9 percent. In FY 2013, total volume decreased from 69.640 billion pieces to 66.538 billion pieces (4.5 percent), but unit contribution increased from 22.16 cents to 23.28 cents (5.1 percent).[22] As a class, First-Class Mail has a very strong coverage and provides a significant contribution to institutional costs ($15.49 billion or 72.74 percent of the overall contribution provided by Market Dominant Mail products).[23]

1. Parcels

The cost coverage for First-Class Parcels fell slightly from 98.5 percent in FY 2012 to 97.2 percent in FY 2013. This decrease in cost coverage of 0.7 percent is significantly less than the decrease this product experienced in FY 2012 when cost coverage fell by 11.5 percent (from 110.0 percent to 98.5 percent).[24] The decrease in cost coverage in FY 2012 was mainly due to the transfer of the most profitable part of First-Class Parcels to the competitive product list. The remaining portion of Parcels had lower cost coverage than the commercial portion.

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[21] USPS-FY13-1.

[22] *Id.;* 2012 ACD at 80-81,

[23] USPS-FY13-1.

[24] *Id.* and 2012 ACD at 81.

The Commission has urged the Postal Service to improve cost coverage for First-Class Parcels “through cost reductions and future rate adjustments”. 2012 ACD at 17. However, in FY 2013, for First-Class Parcels cost per piece increased by 20 cents - from $2.21 to $2.4. Although in January 2013, prices for First-Class Mail Parcels increased on average by 5 percent, the product still remains under water.[25] In January 2014, the Postal Service implemented another price increase for First-Class Mail Parcels, which, as the Postal Service has noted, should bring the cost coverage of First-Class Parcels for FY 2014 to a level above 100 percent. 2013 ACR at 11.

2. Inbound Single-Piece

The Postal Service argues that failure of Inbound Single-Piece First-Class mail to cover its attributable costs is due to “the product’s unique pricing regime,” and its inability to independently set prices for delivering foreign origin mail. The Postal Service expresses hope that a new terminal dues formula for setting prices effective January 1, 2014 will have a positive effect on revenue and cost coverage. *Id.* This new formula is a result of long-term negotiations, and, as the Commission has noted, it “should significantly improve cost coverage” for Inbound Single-Piece First Class mail product. 2012 ACD at 17.

Given the Postal Service’s transfer of parcel products during FY 2012 and the pricing regime for inbound single-piece, the Public Representative does not believe First-Class Mail rates were out of compliance in FY 2013 with provisions of Chapter 36 of title 39.

B. Standard Mail Cost Coverage

The Standard Mail class is the largest mail class by volume, representing more than half (52.1 percent) of all Market Dominant mail volume and 29.9 percent of the total

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[25] 2012 ACD at 81 and USPS-FY13-1.

market dominant products' contribution to institutional costs.[26] In FY 2013, there was an increase in both the percentage of Standard Mail in market dominant mail volumes (1.4 percent) and its share of the market dominant products' contribution to institutional costs (2.7 percent).[27] Standard Mail volumes slightly increased in FY 2013 by 1.01 percent.[28] In FY 2013, the cost coverage increased substantially, moving up by 10 percent, from 149 percent to 159 percent. In the two previous years, it also increased by 1.4 in FY 2012 and 2.6 percent in FY 2011. The overall dollar contribution of Standard Mail to institutional costs was $6.4 billion (compared to $15.5 billion for First-Class Mail). *Id*

In FY 2013, volumes declined for Standard Flats and for High-Density and Saturation Flats and Parcels (by 6.3 percent and 3.7 percent respectively) and increased for Carrier Route (by 4.2 percent), High Density and Saturation Letters (by 2.7 percent) and Letters (by 1.5 percent). Standard Mail Parcels mail volumes declined substantially - by 76.1 percent. *Id.* The volume decline was not the result of falling demand but was mostly because, on January 22, 2012, the significant portion of mail in this subclass (previously named Standard Mail Non-Machinables and parcels) was moved to the competitive product list.[29]

Standard Mail Negotiated Service Agreement (NSA) mail volume that increased by almost 4.5 times in FY 2012 was stable in FY 2013. The Public Representative acknowledges the continuing increase in Standard Mail NSAs cost coverage per piece, which moved from 163.84 percent in FY 2011 to 189.74 percent in FY 2012 to

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[26] Calculated using data from USPS-FY13-1.

[27] *Id* and Docket No. ACR2012, PRC-ACR2012-LR1.

[28] In FY 2012 Standard Mail declined by 5.8 percent, while in FY 2011 it increased by 1.03 percent. *See* USPS-FY13-1; Docket No. ACR 2012, PRC-ACR2012-LR1; Docket No. ACR 2011, PRC-ACR2011-LR1.

[29] *See* Docket No. MC2010-36, Order Conditionally Granting Request to Transfer Commercial Standard Mail Parcels to the Competitive Product List, March 2, 2011 (Order No. 689); Docket No. CP2012-2, Order Approving Changes in Rates of General Applicability for Competitive Products, December 21, 2011 (Order No. 1062).

229.99 percent in FY 2013. Per piece Standard Mail contribution to institutional cost increased by 19.2 percent (4 percent more than in FY 2012).[30]

On September 7, 2012, the Commission approved the Postal Service request to add a new market dominant product – Every Door Direct Mail Retail to the product list.[31] In FY 2013, the cost coverage of this new product was 359.9 percent.[32] However, taking into account a very small share of both Standard Mail NSA and Every Door Direct Mail Retail volumes in overall Standard Mail volumes (each share constitutes a little more than 1 percent), their cost coverage could not have had any visible effect on overall Standard Mail class cost coverage.

The majority of Standard Mail products (except Standard Flats and Standard Parcels) have over 100 percent cost coverage, ranging from 133.4 percent to 359.9 percent. Standard Flats and Standard Parcels provide negative contribution to the institutional costs which raises a concern about compliance with Section 3622(c)(2) of title 39, as discussed below.

1. Standard Parcels

In FY 2013, Standard Parcels unit contribution fell to less the half the previous years' contribution, and cost coverage declined by 20 percentage points (from 85.5 percent to 64.3 percent).[33] The Public Representative agrees with the Postal Service that this product now has a larger portion of nonprofit mail which would account for the decline in cost coverage. 2013 ACR at 18. In the Public Representative's Initial Comments on FY 2012 ACR, the Public Representative recommended the Postal

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[30] *See* USPS-FY13-1; Docket No. ACR2012, PRC-ACR2012-LR1; Docket No. ACR2011, PRC-ACR2011-LR1.

[31] Docket No. MC2012-31, Order Approving Addition of Postal Services to the Mail Classification Schedule Product List, September 7, 2012 (Order No. 1460).

[32] USPS-FY13-1.

[33] Calculated using data from USPS-FY13-1 and 2012 ACD at 117.

Service carefully monitor cost coverage for that product and “develop measures to foster an increase in the product cost coverage.”[34] In its FY 2012 ACD report, the Commission encouraged the Postal Service to reduce Parcels costs in order “to close the cost coverage gap.” 2012 ACD at 117. In FY 2013, following the substantial decrease in volume, Standard Mail Parcels total attributable costs fell to less than one third of FY 2012 costs. While in FY 2012, the share of Standard Mail Parcels of the total costs for Standard Mail was 3 percent, in FY 2013 it fell to only one percent.[35] This has diminished the overall Standard Parcels institutional burden of the Postal Service. The Public Representative believes that the Postal Service is on the right track in the measures undertaken to improve cost coverage, including proposed “above average price increases in future price adjustments.”

2. Standard Flats

As for Standard Flats, its volumes declined by 6.3 percent in FY 2013. This decline is less than the decline in FY 2012, when volume fell by 12.5 percent. While volume for Standard Flats declined in FY 2013, its cost coverage increased by 4 percent (from 80.9 percent to 84.9 percent). The increase in cost coverage is higher than in the previous year, when only a slight increase of 1.4 percent was observed.[36] Contribution of Standard Flats to institutional costs, while still negative, continued to improve. Per piece contribution increased from a loss of 8.9 cents to a loss of 6.8 cents (an improvement of over 24 percent), and the overall Standard Flats contribution to the institutional burden of the Postal Service decreased from $528 million to $380 million, or more than 28 percent. This is a significant improvement from last year when per piece contribution increased by 5 percent only (from a loss of 9.47 cents to a loss of 8.89 cents), and contribution to the institutional burden decreased by 18 percent. *Id.*

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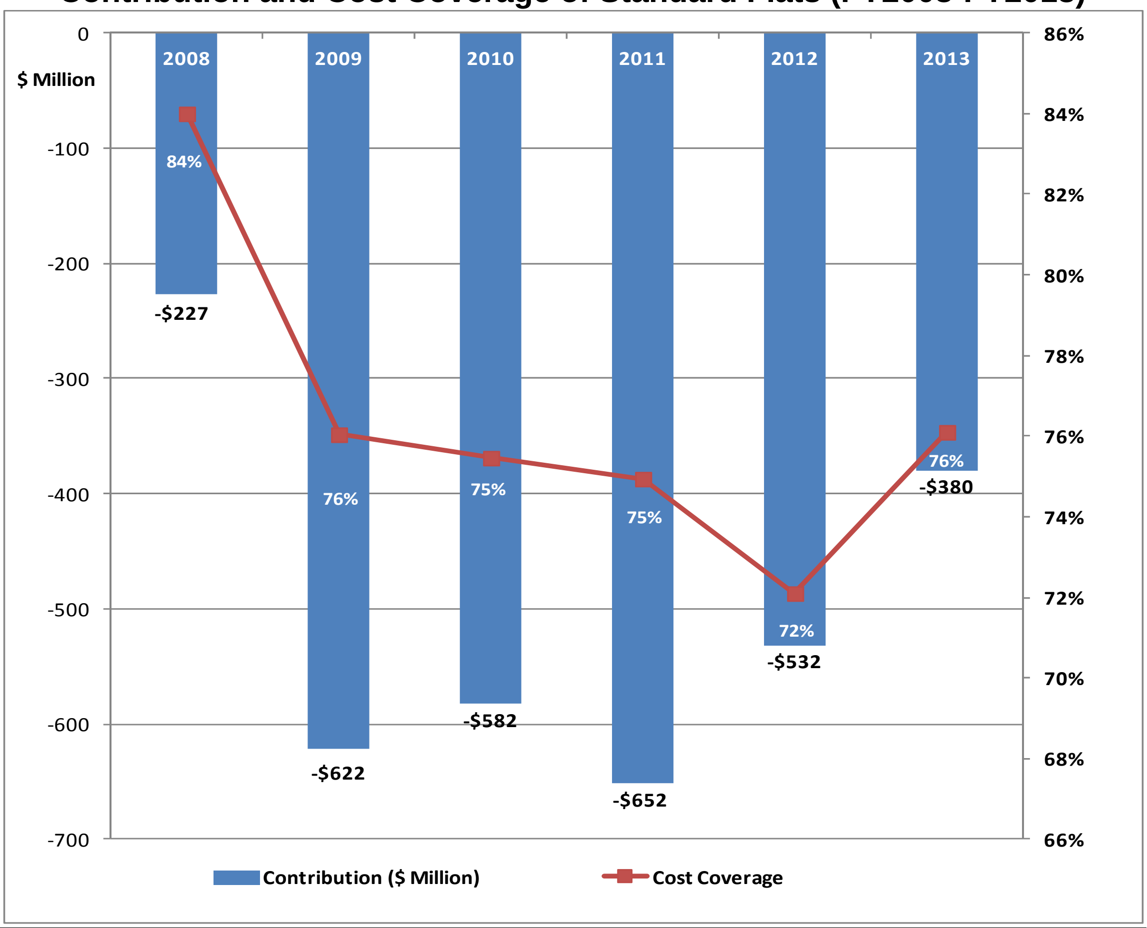
[34] Docket No. ACR2012, Public Representative Initial Comments at 29.

[35] USPS-FY13-1; 2012 ACD at 106 and 2011 ACD at 112.

[36] In FY 2012, Standard Flats cost coverage increased from 79.5 to 80.9 percent. *Id*

Chart V-1, below illustrates the observed decrease in the institutional burden over the last two years. The Public Representative recognizes that the Postal Service continues to undertake multiple operational changes in order to reduce Standard Mail Flats costs, as directed by the FY 2010 ACD.[37] In the FY 2012 ACD, the Commission acknowledged that the Postal Service began "to make progress towards addressing the issues raised by the Commission in FY 2010 ACD" and confirmed that the Postal Service should continue to follow FY 2010 ACD directives.[38]

Chart V-1
Contribution and Cost Coverage of Standard Flats (FY2008-FY2013)



[37] 2010 ACD at 107.

[38] 2012 ACD at 116.

Data Source: Responses of the United States Postal Service to Question 2 of Chairman's Information Request No. 1, January 23, 2014, Question 1c.

The Postal Service has reported a number of operational changes introduced in FY 2013 in order to reduce costs of Standard Flats.[39] Continued improvement in cost coverage for Standard Flats proves the effectiveness of a "special remedy", *i.e.* above CPI price increases for Standard Mail Flats.

3. Elasticity

In the Public Representative's initial comments to ACR 2012, the Public Representative noted that "over the observed years, the Standard Mail products have become more elastic; and it is reasonable to assume that this trend is likely to continue in the near future".[40] The comparison of changes in own price elasticity estimated by the Postal Service in FY 2011-FY 2013 (*see* Table V-2 below), shows that this statement is still valid for all Standard Mail products except, probably, Standard ECR Nonprofit.

Table V-2
FY 2011-FY2013 Own-Price Elasticities of Demand for Standard Mail

	January 2011[1]	January 2012[2]	January 2013[3]	September 2013[4]
Standard Regular	-0.286	-0.335	-0.437	-0.464
Standard ECR	-0.727	-0.782	-0.704	-0.888
Standard Nonprofit	-0.177	-0.265	-0.299	-0.374
Standard ECR Nonprofit	-0.513	-0.542	-0.560	-0.430

[1.] Market Dominant Products: USPS Demand Equation Estimation and Volume Forecasting Methodologies. January 20, 2011.
[2] Demand Analyses FY 2012 – Market Dominant, January 22, 2013.
[3] Demand Analyses and Volume Forecast Materials for market Dominant Products. January 20, 2012
[4] Docket No. R-2013-11, USPS-R2010-4R-9, September 26, 2013.

During the years reported in the above Table V-2, the Postal Service has been estimating own price elasticity for all Standard Regular mail, but has not estimated

[39] *See* Responses of the United States Postal Service to Chairman's Information Request No. 2, January 23, 2014, question 1a.

[40] Docket No. ACR2012, Public Representative Initial Comments at 35.

elasticity by product. However, in the FY 2012 ACD, the Commission noted that it would be useful to have own-price elasticities of demand for Standard Mail available by product. In regard to Standard Flats, in the FY 2012 ACD, the Commission recommended "that the Postal Service derive elasticity estimates to provide for a more realistic assessment of the impact of price changes on contribution." 2012 ACD at 116. In its FY 2013 ACR, the Postal Service has not followed the Commission's recommendation and still estimates own price elasticity for all Standard Mail without any differentiation by product. Consequently, the elasticity for Standard Flats is unknown, and is assumed to be the same as for overall Standard Mail Regular and other Standard Mail Regular products.

The Postal Service's failure to provide elasticities for products is a strong disadvantage. In FY 2013 ACR, the Postal Service is planning prices for Standard Flats for FY 2015 and FY 2016 in accordance with the schedule of above average price increase (5 percent above CPI), without any considering price elasticity. As the Public Representative pointed out in its FY 2012 ACR Reply Comments, the Postal Service should employ a demand-based pricing policy when setting prices for Standard mail products.[41] This should insure the greater product contribution to institutional costs, and a positive effect of such rate increases on the general public and other mail users in accordance with 39 U.S.C. § 3622(c)(3).

C. Periodicals Cost Coverage

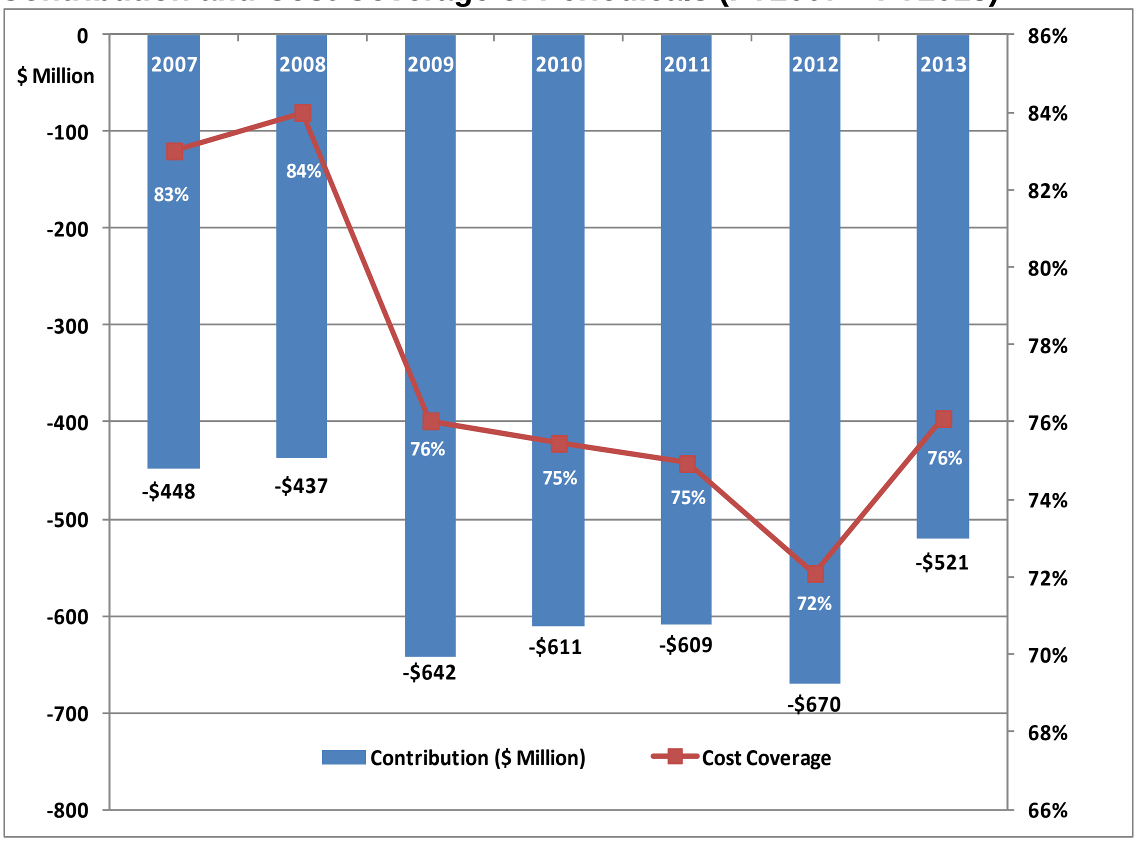
In FY 2013, Periodicals again failed to cover their attributable costs. This is consistent with results for the years since enactment of the PAEA in 2006. In FY 2013, Periodicals volume declined by 5.7 percent, consistent with the decline from FY 2008 through FY2012 when the annual rate of volume decline ranged between 2.2 and 8.6 percent).[42] However, cost coverage has increased by 4 percent (from 72.1percent

[41] Docket No. ACR2012, Public Representative Reply Comments at 22.

[42] USPS-FY13-1 and 2012 ACD at 93.

to 76.1 percent) – breaking the tendency of consistent decline in cost coverage (see Chart V-2 below).

Chart V-2
Contribution and Cost Coverage of Periodicals (FY2007 – FY2013)



Source: ACD 2012 at 93 and USPS-FY13-1.

As shown in Chart V-2 in FY 2013, the contribution to the institutional burden decreased from $670 million to $520 million, or over 22.2 percent. Although, a one year improvement in the financial results does not yet provide a solid ground for positive conclusions, it gives some hope. The increase in cost coverage for both Periodicals products – In County and Outside County[43] represents a positive shift in direction. On February 14, 2013, in Order No. 1656 the Commission approved the changes to the

[43] In FY 2013, cost coverage increased by almost 5 percent for In County Periodical Mail (from 70.57 percent to 75.2 percent) and by 3.5 percent for Outside County Periodical Mail (from 72.2 to 75.8 percent). *See* USPS-FY13-1 and Docket No. ACR2012, PRC-ACR2012-LR1.

Periodicals cost model proposed by the Postal Service in Docket No. RM2012-8.[44] In the 2011 Periodicals Cost Study, the Commission expresses the concern that "the unit cost of Periodicals mail…has risen in real terms since FY 1990.[45] However, In FY 2013 the unit cost of Periodicals was 34.30 cents, which is 3.7 less than in FY 2012 and 1.2 percent less than in FY 2011.[46]

The Public Representative acknowledges both the decrease in unit costs and increase on cost coverage of Periodicals in FY 2013. However, the one year improvement will still require the continued monitoring and reporting of Periodicals cost coverage. The Public Representative respectively requests the Commission to direct the Postal Service to continue implementing cost savings and productivity improvement measures.

D. Package Services

In FY 2013, cost coverage for Package Services overall was 101.2 percent. Revenue was just 1.2 percent above attributable costs. However, in FY 2013, overall class cost coverage is 4.5 percent higher than in FY 2012, when Package Services failed to cover their attributable costs. Cost per piece decreased from $2.54 in FY 2012 to $1.96 (22.8 percent) in FY 2013, but revenue per piece also decreased, although at a little lower rate, from $2.49 cents to $1.99 cents (20.1 percent). In FY 2013, two Packages Services products (Parcel Post and Media Mail/Library Mail) still failed to

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[44] Docket No. RM2012-8, Order on Analytical Principles Used in Periodic Reporting (Proposal Nine), February 14, 2013 (Order No. 1656).

[45] Periodicals Mail Study. Joint Report of the United States Postal Service and Postal Regulatory Commission. September 2011 at 97. *See* http://about.usps.com/postal-act-2006/periodicals-mail-study.pdf

[46] Unit cost coverage of Periodicals was 35.62 cents in FY 2012 and 35.34 cents in FY 2011. *See*: USPS-FY13-1; Docket No. ACR2012, PRC-ACR2012-LR1 and Docket No. ACR2011, PRC-ACR2011-LR1.

cover its attributable costs. Cost coverage for the other four Package Services products was in the range between 104.25 percent and 208.49 percent.[47]

1. Parcel Post

In FY 2013, cost coverage for [Single-Piece] Parcel Post was 96.1 percent.[48] This number actually reflects the financial results for the part of FY 2013, up to January 27, 2013.[49] On this date, Parcel Post was moved from market dominant to the competitive product list, leaving Alaska Bypass Service as a stand-alone product of Package Services.[50] In FY 2013, cost coverage for Single-Piece Parcel Post was 3.9 percent higher than in FY 2012.

As for Alaska Bypass Service, it covered its attributable costs in FY 2013 (cost coverage was 208.9 percent).[51] FY 2013 financial worksheets with data on the Standard Post competitive product (the other successor of Single-Piece Parcel Post) do not appear to raise a concern about cost coverage.[52]

The Public Representative believes that the applicable rates for the products in the changed product list are reasonable and should lead to further improvement of cost coverage for products that are successors of Single-Piece Parcel Post.

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[47] USPS-FY13-1 and 2012 ACD at 128.

[48] USPS-FY13-1.

[49] *See* Responses to the United States Postal Service to Chairman's Information Request No. 1, January 13, 2014, question 12.

[50] On January 27, 2013, the product named Single-Piece Parcel Post was eliminated and separated into two currently existing products – Standard Post (which was transferred to the competitive list as Parcel Select, and then renamed) and Alaska Bypass Service which was added to the market dominant list. *See* Docket No. MC2012-13, Order Conditionally Granting Request to Transfer Parcel Post to the Competitive Product List, July 9, 2012 (Order No. 1411) and Docket No. CP2013-3, Order Approving Changes in Rates of General Applicability for Competitive Products, November 8, 2012 (Order No. 1536).

[51] USPS-FY13-1 and FY 2012 ACD at 128.

[52] USPS-FY13-NP11.

2. Media Mail/Library Mail

In FY 2013, Media Mail/Library Mail did not cover its attributable costs. The product cost coverage was 84.2 percent – 1 percent lower than in FY 2012 (when it was 85.3 percent).[53] The Postal Service is planning to increase cost coverage for Media Mail/Library Mail to 94.3 percent by putting into effect the exigent prices proposed in R2013-11.[54] Such measure is consistent with the Commission recommendation to "continue pricing Media Mail/Library Mail in a way that improves cost coverage." 2012 ACD at 130. However, even if in FY 2014 the Postal Service reaches its goal regarding the product cost coverage, Media mail/Library Mail will still remain under water. Taking into account that Media Mail/Library Mail has consistently failed to cover attributable costs,[55] the product requires special attention. In the FY 2012 ACD, the Commission directed the Postal Service to "discuss the effects of its Network Rationalization effects on Media Mail/Library Mail's unit costs in its FY 2013 ACR."[56] Due to lack of such discussion in the current ACR, the Public Representative performed the comparison between mail processing costs for this product in FY 2013 and FY 2012. The Public Representative concludes that, for all price categories, the unit costs have increased since FY 2012.[57] This raises a significant concern about not only the current compliance of Media Mail/Library Mail with Section 3622(c)(2) of title 39, but also the product's ability to comply with the statutory requirement in FY 2014.

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[53] USPS-FY13-1 and 2012 ACD at 128.

[54] *See* R2013-11, Statement of Stephen Nickerson on Behalf of the United States Postal Service. (Revised on 11/22/13), Attachment 25 (file NickStatmnt.Attach.Rev.1.22.13.xls, tab "Attach 25 2014 Cont 1 AR 26").

[55] *See id* at 129-130.

[56] 2012 ACD at 130. Network Rationalization was the subject of Docket No. N2012-1. See: Advisory Opinion on Mail Processing Network Rationalization Service Changes, September 28, 2012.

[57] USPS-FY13-15, file USPS-FY13-15.MM-LM, tab "Summary" and Docket No. FY2012, USPS-FY12-15, file USPS-FY12-15.MM-LM, tab "Summary".

VI. Worksharing

A. First-Class

In Docket No. ACR FY2012, the Public Representative stated that "[i]n every ACR, the Postal Service has reported twenty or more, non-ECSI, passthroughs greater than 100 percent. This year [FY 2012], it reports twenty-one such passthroughs." Comments of the Public Representative, Docket No. ACR2012 at 40. This year [FY2013] is no exception. The Postal Service reports 20 non-ECSI passthroughs greater than 100 percent, and two negative passthroughs. Table VI-1, Non-ECSI Passthroughs Above 100 percent, lists the products receiving discounts above the costs they avoid.

Table VI-1
Non-ECSI Passthroughs Above 100 Percent

Mail	Percent
First Class	
Single Piece Letters, QBRM	113.3
First-Class Mail, Single Piece Cards, QBRM	113.3
Mixed AADC Automation Letters	103.8
Mixed AADC Automation Cards	176.9
ADC Automation Flats	140.8
3-digit Automation Flats	127.8
5-digit Automation Flats	133.3
Automation 3-digit Flats	121.3
Automation 5-digit Flats	144.4
Standard	
Nonautomation ADC Nonmachinable Letters	135.7
Nonautomation 3-Digit Nonmachinable Letters	161.9
Nonautomation 5-digit Nonmachinable Letters	137.7
Automation 3-digit Flats	117.9
Automation 5-digit Flats	108.1
Automation, Mixed AADC Flats	305.6
Nonautomation 3-digit Flats	142.9
Nonautomation 5-digit Flats	132.2
Parcels & Marketing Parcels, Mixed NDC Irregular Parcels	187.2
Parcels & Marketing Parcels, Mixed NDC Machinable Nonbarcoded Parcels	182.9

Parcels & Marketing Parcels, Mixed NDC Irregular Nonbarcoded Parcels	182.9
Mixed NDC Barcoded Marketing Parcels	182.9
NDC Irregular Parcels	187.2
NDC Marketing Parcels	135.5
Package Services	
Basic, Carrier Route DNDC Flats	121.4
Basic, Carrier Route DNDC Parcels / IPPs	121.4

Source: USPS-FY13-3.Workshare, Filename.xlsx

1. First Class QBRM

The relevant portions of Table VI-2 are reproduced below for convenient reference.

Table VI-2
First Class QBRM, Letters, and Cards Passthroughs Above 100 Percent

Mail	Percent
First-Class, Single Piece Letters, QBRM	113.3
First-Class Mail, Single Piece Cards, QBRM	113.3
First-Class, Mixed AADC Automation Letters	103.8
First-Class, Mixed AADC Automation Cards	176.9

Last year, the Commission found that First Class, QBRM Letter and Card discounts greater than avoided costs were not justified by any statutory exceptions, and stated that it expected greater alignment of avoided costs and discounts after the price changes in R2013-1. 2012 ACD at 83. Although these passthroughs have come down from 129.4 percent to 113.3 percent this year, they remain higher than 100 percent. The Postal Service’s intent to better align avoided costs and discounts has traditionally been accepted by the Commission as an appropriate response to excessive passthroughs, even if the Commission has determined the Postal Service has not offered sufficient explanation to warrant the application of a statutory exemption from section 3622 of title 39.

This year’s passthrough represents more efficient pricing, and it will appear to become more so once exigent price increases take effect. No further action is warranted at this time, but the Public Representative observes that the rate changes due to exigent rate increases are scheduled to disappear in two years.

2. First-Class, Mixed Automation AADC Letters and Cards

Table VI-3
First Class Flat Passthroughs Above 100 Percent

Mail Class	Percent
ADC Automation Flats	140.8
3-digit Automation Flats	127.8
5-digit Automation Flats	133.3
Automation 3-digit Flats	121.3
Automation 5-digit Flats	144.4

Last year, the Commission found that the discounts for First-Class-Mixed Automation AADC Letters were greater than avoided costs, and were not justified by any statutory exceptions. The Commission stated that it expected greater alignment of avoided costs and discounts after the price changes in Docket No. R2013-1. 2012 ACD at 84.

This year's passthrough represents more efficient pricing, and will temporarily become more so, once exigent price increases take effect. Table VI-3. No further action is warranted at this time, but the Public Representative notes that the rate changes due to the exigent rate increases are scheduled to disappear in two years.

3. First Class Automation Flats

Last year, the Commission found that the discounts for the three First-Class Automation Flat products, were greater than avoided costs. The discounts were not justified by any statutory exceptions, but the Commission expected greater alignment of avoided costs and discounts after the price changes in Docket No. R2013-1. 2012 ACD at 87. This year passthroughs have increased, with the exception of Automation ADC Flats, which is still 140.8 percent.

The Public Representative sees no reason to accept the Postal Service's argument that it will bring passthroughs this high closer to 100 percent in the future. It is very likely that the annual volatility of unit avoided costs will prevent the Postal Service from improving alignment next year.

Automation ADC Flats. Although the passthrough for Automation ADC Flats has been reduced from 158.7 to 140.8 percent, the Public Representative believes it is unlikely further progress will be made once the exigent price increases are terminated. Nevertheless, the Postal Service has recently reduced this passthrough and the Commission has traditionally accepted this as reason to not take further action.

Automation 3-digit Flats. The Postal Service suggests that the volatility of passthroughs accounts for the increase this year in the passthrough of Automation 3-digit Flats. It proposes bringing this product's discount and avoided unit cost into closer alignment in the future. 2013 ACR at 14. It does not provide a statutory exception to justify the Automation 3-digit Flat passthrough.

Automation 5-digit Flats. The Postal Service also contends that it set the discount for Automation 5-digit Flats at a level that would reproduce the previous years' passthrough. Unfortunately, unit avoided costs declined over 4 cents since setting the discount, which causes the passthrough to increase to 133.3 percent. Because the Postal Service would have to reduce this discount by 4 cents (or by about 1/4th of the total discount) in order to reduce the passthrough to 100 percent, the Postal Service justifies the passthrough pursuant to the rate shock exemption in section 3622(e)(2)(B). The Postal Service contends it will bring discounts into closer alignment with avoided costs over time, albeit perhaps more slowly than might be the case for other products. USPS Final Notice at 14.

The Postal Service explains that it cannot bring this passthrough to 100 percent without raising the rate and causing rate shock. It explains that it is administratively unable to actually implement this rate increase due to timing and regulatory issues, but if it were able to do so, rate shock would occur and automation 5-digit flats qualify for an exemption pursuant to section 3622(e)(2)(B). Responses of the United States Postal Service to Chairman's Information Request No. 2, question 11. The Public Representative sees no need for the Postal Service to rely upon the rate shock section 3622(e)(2)(B) since it maintains that it would be infeasible to alter rates and would only be rate shock if it were able to alter rates. Section 3622(e)(2)(B)(i) does not contemplate "hypothetical" or "virtual" rate shock.

B. Outside County Periodicals

Ten out of 21 Outside County Periodical products, have discounts greater than avoided costs and another two products have anomalously large negative passthroughs. Periodicals qualify for the ECSI exemption, but the Commission has urged the Postal Service to use the pricing of bundles, sacks and containers, to incent mailers to more efficiently prepare Periodical Mail. 2012 ACD at 101. The Postal Service has reduced bundle, sack and pallet price cost ratios across the board this year. The Public Representative concludes that the Postal Service has taken the Commission's suggestion into consideration.

C. Standard Mail Letters

There are three Standard Mail Letter products with passthroughs greater than 100 percent: Nonautomation ADC Nonmachinable Letters, Nonautomation 3-Digit Nonmachinable Letters, and Nonautomation 5-digit Nonmachinable Letters. Passthroughs range from a low of 135.7 percent for Nonautomation ADC Nonmachinable Letters, to a high of 161.9 percent for Nonautomation 5-digit Nonmachinable Letters.

Table VI-4
Standard Mail Letter Passthroughs Above 100 Percent

Mail	Percent
Nonautomation ADC Nonmachinable Letters	135.7
Nonautomation 3-Digit Nonmachinable Letters	161.9
Nonautomation 5-digit Nonmachinable Letters	137.7

1. Nonautomation ADC Nonmachinable Lettes

The Postal Service does not offer a statutory exception for Nonautomation ADC Nonmachinable Letters, but notes that an unexpected reduction in avoided costs (volatility) is responsible for increasing the passthrough from 116.3 in Docket No. R2013-10. The Postal Service states that it had been making progress reducing the passthrough to 100 percent, and implies the Commission should accept its promise to improve alignment in the future. 2013 ACR at 20. The Public Representative does not believe the Postal Service is able to bring discounts into better alignment with avoided costs, because it seems to have little, if any, control over avoided costs. It is able to slightly reduce discounts, but recent history has shown that avoided cost changes (usually reductions) regularly overwhelm discount reductions and yield increasing, not decreasing, passthroughs.

2. Nonautomation 3-Digit and 5-Digit Nonmachinable Letters

The Postal Service argues that the increased passthrough for Nonautomation 3-digit Nonmachinable Letters and Nonautomation 5-digit Nonmachinable Letters, qualify for two exemptions: incentivizing more finely presorted mail (section 3622(e)(2)(D)), and rate shock (3622(e)(2)(B)). Rate shock would occur since bringing these passthroughs equal to 100 percent would require a reduction in their discounts by approximately 20 percent. 2013 ACR at 20. The Commission should not exempt these products pursuant to 3622(e)(2)(B) for the reasons explained with respect to First-Class Automation Flats.

The Postal Service also argues that this excessive passthrough incents mailers to enter mail at a more finely presorted level, which would qualify 3-digit Nonmachinable Letters for an exemption pursuant to 3622(e)(2)(D). The Public Representative supports more efficient mail preparation, but is concerned that the Postal Service has not provided any evidence on how much excessive passthroughs, and not other factors, are responsible for improved mail preparation. The Commission should permit excessive passthroughs pursuant to 3622(e)(2)(D) only when there is evidence that the increased utilization of the discount results in a substantial reduction in avoided cost. The Public Representative also recommends the Postal Service and/or the Commission investigate whether or not there are diminishing marginal benefits from continued and/or increasing passthroughs greater than 100 percent for a product.

3. Standard Mail Flats

Table VI-5
Standard Flat Passthroughs Above 100 Percent

Mail	Percent
Automation 3-digit Flats	117.9
Automation 5-digit Flats	108.1
Automation, Mixed AADC Flats	305.6
Nonautomation 3-digit Flats	142.9
Nonautomation 5-digit Flats	132.2

There are five Standard Mail Flats products with passthroughs greater than 100 percent: Automation Mixed AADC Flats, Automation 3-digit Flats, Automation 5-digit Flats, Nonautomation 3-digit Flats, and Nonautomation 5-digit Flats. Passthroughs range from a low of 108.1 percent for Automation 5-digit Flats, to a high of 305.6 percent for Automation Mixed AADC Flats. Table VI-5. The Postal Service explains that the increase in passthroughs or passthroughs above 100 percent is the result of efficiency improvements which have caused the unit avoided costs for these products to decline. The Postal Service seeks a “rate shock” exemption pursuant to section

3622(e)(2)(B) because it would require a significant reduction in the discounts in order to bring passthroughs equal to 100 percent. 2013 ACR at 27.

The Postal Service also contends that the excessive passthrough for Automation Mixed ADC Flats will continue to incent mailers to prebarcode flats so that they may be sorted on an FSS machine. The Postal Service contends that "there still continues to be a need for a pre-barcoding incentive…." *Id*. The Postal Service does not provide any evidence on the level of discount needed, nor does it explain why an *increase i*n the passthrough from 239 percent to 306 percent is needed. In other words, it does not explain why a passthrough of 239 percent is insufficient a year after the deployment of FSS has been completed. The Postal Service should provide this evidence in order for this discount to qualify for an exemption pursuant to 3622(e)(2)(D).

4. Standard Mail Parcels

Table VI-6
Standard Parcel Passthroughs Above 100 Percent

Mail Class	Percent
Parcels & Marketing Parcels, Mixed NDC Irregular Parcels	187.2
Parcels & Marketing Parcels, Mixed NDC Machinable Nonbarcoded Parcels	182.9
Parcels & Marketing Parcels, Mixed NDC Irregular Nonbarcoded Parcels	182.9
Mixed NDC Barcoded Marketing Parcels	182.9
NDC Irregular Parcels	187.2
NDC Marketing Parcels	135.5

Six Standard Mail Parcel passthroughs exceed 100 percent: Mixed NDC Irregular Marketing Parcels, Mixed NDC Machinable Nonbarcoded Marketing Parcels, Mixed NDC Irregular Nonbarcoded Marketing Parcels, Mixed NDC Barcoded Marketing Parcels, NDC Irregular Parcels, and NDC Marketing Parcels. Except for NDC Marketing Parcels (135.5 percent, all are above 180 percent.

The Postal Service notes that the passthrough for NDC Irregular Parcels is 187.2 percent, down from 242.8 percent in FY 2012. The Postal Service contends that bringing the passthrough immediately to 100 percent would require a substantial decline in the discount, which would effectively result in a nearly 20 percent rate increase. 2013 ACF at 28. It seeks an exemption for this excessive passthrough pursuant to section 3622(e)(2)(B) in order to avoid rate shock.

As stated above, the Public Representative sees no need for the Postal Service to rely upon 3622(e)(2)(B) when it claims it is unable to modify prices. If rate shock is not possible, then the exemption for an excessive passthrough pursuant to 3622(e)(2)(B) should not be available.

The Postal Service's argues that the excessive passthroughs for Mixed NDC Machinable Barcoded Parcels, Mixed NDC Irregular Barcoded Parcels, and NDC Marketing Barcoded Parcels will continue to incent parcel mailers to prepare their mail so that it may be sorted on mechanized parcel sorting machines. It seeks exemption for these excessive passthroughs pursuant to the efficient operation exemption in section 3622(e)(2)(D). The Public Representative notes that the same passthroughs were 164.1 percent last year. Since the passthrough has remained relatively constant compared to last year, the PR accepts the Postal Service's proposed exemptions.

5. Media Mail and BPM Mail

Four discounts from these mail categories have passthrough that exceeded 100 percent in FY 2013: Media Mail Basic, Library Mail Basic, BPM Flats and BPM Parcels Parcels DNDC dropship discounts.[58] 2013 ACR at 35. Media and Library mail qualify for an ECSI exemption pursuant to 39 U.S.C. § 3622(e)(2)(C). The Postal Service states that the 2 Bound Printed Matter passthroughs will decline to 100.7 percent January 26, 2014 (once rates determined in Docket No. R2013-11 take effect). The Postal Service also states that it will "further align the discounts with the cost avoidance in the next price adjustment." 2013 ACR at 35.

[58] *See* Table VI-1

The Public Representative recognizes the ECSI exemption for Media and Library Mail, but is skeptical of the Postal Service's ability to reduce the excessive passthroughs for BPM Flats and BPM Parcels DNDC dropship discounts by bringing avoided costs and discounts into better alignment. The Postal Service acknowledges there is a high year-to-year volatility in avoided costs. Furthermore, once the exigent rate increases are withdrawn, the Postal Service's discount flexibility will be more restricted

D. Worksharing Conclusion

The number of products with passthroughs greater than 100 percent has declined this year from 21 to 20 which does not seem to be a real improvement. Volatile avoided costs continue to be an obstacle towards reducing excessive passthroughs in the following year since the Postal Service sets discounts before it knows avoided costs for products. As a result, improvements in passthroughs will be largely due to chance until the Postal Service is better able to estimate its avoided costs for the year.

The Postal Service has also unnecessarily relied upon section 3622(e)(2)(B) in order to justify excessive passthroughs.

Finally, the Public Representative believes there are diminishing returns to increasing the incentive to improve mail preparation. This is an issue that deserves further examination.

VII. COMPETITIVE PRODUCTS

As mandated by 39 U.S.C. § 3633(a), the Commission's regulations in 39 C.F.R. § 3015.7 require that:

- Market dominant products do not subsidize competitive products (39 U.S.C. § 3633(a)(1));

- Each competitive product covers its attributable costs (39 U.S.C. § 3633(a)(2)); and
- Competitive products collectively cover an appropriate share of the Postal Service's institutional costs (39 U.S.C. § 3633(a)(3)).

The Public Representative finds the requirements of 39 U.S.C. § 3633(a)(1) and (3) have been satisfied in FY 2013 based on the information provided by the Postal Service. However, the Public Representative finds that several competitive products failed to cover their attributable costs in FY 2013. Below the Public Representative discusses concerns and recommendations regarding each competitive product that failed to cover its costs.

A. Market Dominant Products did not Subsidize Competitive Products in FY 2013.

In order to test for compliance with 39 U.S.C. § 3633(a)(1), the Commission applies the cross-subsidy test set forth in 39 C.F.R. § 3015.7(a). In Order No. 399, the Commission approved a hybrid incremental cost methodology for this test. Under that methodology, incremental costs for domestic competitive products, attributable costs for international competitive products, and group specific costs are aggregated to calculate the hybrid incremental cost total for competitive products.[59] The total hybrid incremental costs for competitive products must be lower than the total revenue for competitive products in order to satisfy 39 U.S.C. § 3633(a)(1).

In FY 2013, the total hybrid incremental costs for competitive products were $9.943 billion. 2013 ACR at 47. In FY 2013, the total revenue for competitive products (Competitive Mail and Services) was $13.661 billion.[60] Since in FY 2013 the total

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[59] Docket No. RM2010-4, Order Accepting Analytical Principles Used in Periodic Reporting (Proposal Twenty-Two through Twenty-Five), January 27, 2012, at 4-5 (Order No. 399).

[60] *See* USPS-FY13-LR1, file FY13PublicCRA, tab "Cost3".

competitive products revenue exceeds the total hybrid incremental costs for competitive products, the cross-subsidy test is satisfied and market dominant products did not subsidize competitive products during FY 2013.

However, questions still remain concerning the accuracy of the methodology employed to calculate the total hybrid incremental costs. In Order No. 399, the Commission urged the Postal Service to "work to resolve problems in those areas where incremental costing cannot be currently implemented" and stated that "it is important to make progress toward a comprehensive measure of incremental costs." Order No. 399 at 5. The Public Representative urges the Commission to reexamine the accuracy of the current hybrid costing methodology and investigate whether incremental costs could be developed for international competitive products for future ACRs.

B. Several Competitive Products do not Cover their Attributable Costs.

In order to comply with 39 U.S.C. § 3633(a)(2) and 39 C.F.R. § 3015.7(b), each competitive product must cover its attributable costs. Several competitive products failed to cover attributable costs in FY 2013: (1) Parcel Select;[61] (2) International Priority Airmail (IPA); (3) International Money Transfer Service (Inbound and Outbound); (4) Inbound Air Parcel Post (at non-UPU rates); and (5) Parcel Return Service Contract 4.[62] The Public Representative provides analysis of each product below and in several cases urges the Commission to take action to ensure compliance with 39 U.S.C. § 3633(a)(2) and 39 C.F.R. § 3015.7(b).

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[61] The Postal Service refers to this product as "non-NSA portion of Parcel Select." *See* FY 2013 ACR at 48 and USPS-FY13-NP11, file "FY13Non-PublicCRA.xlsx".

[62] The Postal Service also states that International Return Receipt did not cover its costs in FY 2013. FY 2013 ACR at 48. International Return Receipt is part of the competitive International Ancillary Services product. The International Ancillary Services product covered its costs in FY 2013. In addition, the Commission recently approved a 7.1 percent overall increase in International Return Receipt prices. *See* Docket No. CP2014-5, Order Approving Changes in Rates of General Applicability for Competitive Products, December 12, 2013 at 7 (Order No. 1903).

1. Parcel Select

Parcel Select failed to cover its costs in FY 2013. 2013 ACR at 48. The Postal Service explains that "there are some initial indications that the revenue for this category of mail may be understated" and that the Postal Service "is investigating the potential revenue and costing issues that may be behind the reported Parcel Select cost coverage." *Id.* In Response to CHIR No. 2, questions 3 and 4, the Postal Service explains that in FY 2013, Parcel Select's unit attributable costs and unit transportation costs increased significantly over FY 2012 costs, particularly for non-presort Parcel Select (non-lightweight).[63] One reason the Postal Service cited for the increased unit attributable costs was that "the eligibility requirement for Parcel Select of a minimum volume of 50 pieces was eliminated for mailers shipping Parcel Select Non-Presort and paying by PC Postage." *Id.* question 3. In Order No. 1903, the Commission approved a change to the Mail Classification Schedule that established a minimum volume requirement of 50 pounds or 50 pieces for all Parcel Select Non-Presort. Order No. 1903 at 4, 16.

The Commission should investigate whether Parcel Select's failure to cover costs resulted from an under-reporting of revenue or another data-related anomaly. If no such anomaly is uncovered, the Commission should consider whether additional action is necessary, particularly in light of the new minimum volume requirements for Parcel Select Non-Presort and the 9.2 percent increase in average Parcel Select prices of general applicability as of January 26, 2014. *Id.* at 3, 4 and 16.

2. International Priority Airmail (IPA)

In FY 2013, IPA prices did not cover attributable costs. 2013 ACR at 48. This is the first time IPA has failed to achieve full cost coverage. IPA has regularly covered its

[63] Responses of the United States Postal Service to Questions 1-11 of Chairman's Information Request No. 2, January 23, 2014, questions 3 and 4.

costs and provided a positive contribution to institutional costs.[64] The Postal Service explains that identifying the specific causes of declines in cost coverage for small revenue-reporting products, like IPA, is often difficult on a year-to-year basis. 2013 ACR at 48. As the Postal Service explains, there is no direct observation of the IPA costs. What is actually reported in ICRA as IPA costs is the “small residual portion” of the total IPA “parent” costs. The Postal Service estimates IPA costs by calculating NSA costs, along with drop ship cost savings, and deducting them from total IPA “parent” costs.[65] The Public Representative appreciates the challenges IPA’s relatively low volume[66] may present when assessing IPA’s FY 2013 decline in cost coverage.[67] However, the Public Representative finds that (1) the Postal Service’s definition of IPA “parent product” costs is confusing, and (2) the methodology for calculating IPA costs is undeveloped.

The Public Representative suggests the Commission request the Postal Service to improve its methodology for calculating IPA costs. It should not be ignored that in FY 2013 (as compared to FY 2012), both revenue per piece and overall revenue decreased and overall costs increased. This is of particular concern because the Commission approved a 2.4 percent overall decrease in IPA prices in Docket No. CP2014-5. Order No. 1903 at 6. Therefore, as of January 26, 2014, IPA prices are lower than those that failed to cover costs in FY 2013. The Commission should find that IPA did not comply with 39 U.S.C. § 3633(a)(2) in FY 2013 and order the Postal Service to further investigate the decreases in revenue per piece and overall revenue and

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[64] *See, e.g.*, Docket No.ACR2012, PRC-ACR2012-NP-LR2, file “PRC-ACR2012-NP-LR2_Booked ICRA”, tab “ACR2012 Intl Products Booked”; FY 2011 ACD at 157.

[65] Responses of the United States Postal Service to Chairman’s Information Request No. 3, January 27, 2014, Question 11 (a-b).

[66] As the Postal Service has reported, it is approximately 2 percent of the total “parent product” costs. *Id.*

[67] *See* Docket No. ACR2012, PRC-ACR2012-NP-LR2, file “PRC-ACR2012-NP-LR2_Booked ICRA”, tab “ACR2012 Intl Products’ Booked’”; USPS-FY13-NP2, folder “ICRA13”, subfolder “ICRA Core Files”, file “Reports (Booked)”, tab “A pages (c).”

increase in overall costs. In addition, the Commission should assess whether an increase in IPA rates is necessary, in light of the recent 2.4 percent overall decrease in IPA rates.

3. International Money Transfer Service (IMTS)

Two products fall under International Money Transfer Service: IMTS–Outbound and IMTS–Inbound. In FY 2010, the Commission approved the Postal Service's request to classify IMTS–Outbound and IMTS–Inbound as separate competitive products.[68] In each subsequent ACD, the Commission found that the IMTS (FY 2010) product or the IMTS–Inbound (FY 2011 and 2012) product failed to satisfy the requirements of 39 U.S.C. § 3633(a)(2).[69] In FY 2012, the Commission was concerned that cost and transaction data for IMTS–Inbound were unavailable,[70] and that all volume variable and product specific costs were attributed to IMTS–Outbound. 2012 ACD at 165. The Commission ordered the Postal Service to report on how IMTS – Inbound transaction volumes and attributable costs could be estimated or calculated if Proposal 11 could not be implemented. *Id.* at 166. The Postal Service responded that the separation between IMTS–Inbound and IMTS–Outbound "should not be implemented going forward" and recommended "combining Inbound and Outbound IMTS revenue, volume, and costs to produce more statistically valid numbers."[71]

As in FY 2012, the Postal Service reports no transaction volumes or attributable cost information for IMTS–Inbound for FY 2013. This once again precludes the Commission from assessing whether the IMTS–Inbound product covered attributable costs and complied with 39 U.S.C. § 3633(a)(2). Furthermore, for the first time, the

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[68] Docket No. MC2009-19, Order Approving Addition of Postal Services to the Mail Classification Schedule Products Lists, January 13, 2010 (Order No. 391).

[69] *See* 2010 ACD at 142-43; 2011 ACD at 158; 2012 ACD at 165-66.

[70] Transaction data for IMTS–Inbound was also unavailable in FY 2011. 2011 ACD at 158.

[71] Docket No. ACR 2012, Responses of the United States Postal Service to Commission Requests for Additional Information in FY 2012 Annual Compliance Determination, June 26 2013, at 7.

IMTS–Outbound product failed to cover its attributable costs in FY 2013. Even if the Commission were to adopt the Postal Service's recommendation of "combining Inbound and Outbound IMTS revenue, volume, and costs," IMTS as a whole also failed to cover attributable costs in FY 2013.[72]

The Commission should take further steps to ensure that it has the necessary information to evaluate cost coverage for IMTS–Inbound and IMTS–Outbound in future years. In addition, the Commission should consider whether rate increases are necessary for IMTS–Inbound and IMTS–Outbound. In Order No. 1903, the Commission approved the Postal Service's proposal to leave IMTS–Inbound and IMTS–Outbound rates unchanged in 2014. Order No. 1903 at 7.

4. Inbound Air Parcel Post (at non-UPU rates)

In FY 2012, both the booked and imputed revenues for Inbound Air Parcel Post (at non-UPU rates) failed to cover attributable costs. 2012 ACD at 172. The overall cost coverage for Inbound Air Parcel Post was negatively impacted by the rates applicable to inbound air parcels from EPG member countries. *Id.* The Commission found the situation "unacceptable" because "[t]he continued entry of inbound air parcels at rates that do not cover costs means that domestic mailers are subsidizing the entry of such parcels in competition with private companies engaged in international delivery services." *Id*. The Commission directed the Postal Service "to file a report within 90 days regarding its plans to improve the financial results for Inbound Air Parcel Post (at non-UPU rates) and its plans to add EPG bilateral agreements to the competitive product list." *Id.* In response, the Postal Service stated that it was working to improve the overall performance of inbound air parcels under EPG agreements; that it

[72] *See* USPS-LR-NP2, folder "ICRA13", subfolder "ICRA Core Files", file "Reports (Booked)", tab "A pages (c)."

negotiated increased rates with several countries; and that it implemented a performance action plan to address operational issues for EPG Parcels.[73]

In FY 2013, the booked revenues for Inbound Air Parcel Post (at non-UPU rates) continued to fail to cover attributable costs and continued to be non-compliant with 39 U.S.C. § 407(a)(2) and 39 U.S.C. § 3633(a)(2). 2013 ACR at 49. However, cost coverage for the EPG Countries and the Inbound Air Parcel Post product overall improved dramatically in FY 2013 over last year.[74] In addition, unlike in FY 2012, the imputed revenues for Inbound Air Parcel Post (at non-UPU rates) covered attributable costs in FY 2013.[75]

The Postal Service's progress toward full cost coverage in FY 2013 indicates that the Postal Service has made some of the changes necessary to bring Inbound Air Parcel Post (at non-UPU rates) to full cost coverage. The Commission should continue to monitor Inbound Air Parcel Post (at non-UPU rates) to ensure domestic mailers do not subsidize the entry of parcels in competition with private companies engaged in international delivery services.

5. Parcel Return Service Contract 4

Parcel Return Service Contract 4, the subject of Docket Nos. MC2013-46 and CP2013-60, failed to cover its attributable costs in FY 2013.[76] The Public

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[73] Docket No. ACR2012, Responses of the United States Postal Service to Commission Requests for Additional Information in FY 2012 Annual Compliance Determination, June 26, 2013, at 15.

[74] USPS-FY13-NP2, folder "ICRA13", folder "ICM costing", file "NSA Summary (Booked)."

[75] USPS-FY13-NP2, folder "ICRA13", folder "ICM costing", file "NSA Summary (Imputed)."

[76] The contract became effective on May 9, 2013, one business day after the day on which the Commission issued regulatory approval. *See* Docket Nos. MC2013-46 and CP2013-60, Request of the United States Postal Service to Add Parcel Return Service Contract 4 to Competitive Product List and Notice of Filing (Under Seal) of Unredacted Governors' Decision, Contract, and Supporting Data, April 29, 2013, at Attachment B at 2 (Parcel Return Service Contract 4 Request); Docket Nos. MC2013-46 and CP2013-60, Order Adding Parcel Return Service Contract 4 to the Competitive Product List, May 8, 2013 (Order No. 1711). Thus, the contract was only in effect for part of FY 2013—from May 9, 2013 to September 30, 2013.

Representative's review of the associated non-public workpapers highlighted two major areas of concern: (1) the baseline total costs are higher than the baseline unit revenue for certain types of Parcel Select and Parcel Return Service contracts[77] and (2) this contract has transportation and carrier/delivery costs higher than the baseline.

Parcel Return Service Contract 4 is a three year contract with over two years remaining.[78] Since in FY 2013 the contract failed to cover its attributable costs and comply with the requirements of 39 U.S.C. § 3633(a)(2) and 39 C.F.R. § 3015.7(b), the Public Representative encourages the Commission to order the Postal Service to cancel the contract in accordance with Section III of the contract, which allows the Postal Service to cancel the contract with 30 days' notice to its contracting partner.[79]

C. Competitive Products Collectively Covered an Appropriate Share of the Postal Service's Institutional Costs.

Competitive products must cover "an appropriate share of the institutional costs of the Postal Service." 39 U.S.C. § 3633(a)(3). The Commission has determined "the appropriate share of institutional costs to be recovered from competitive products collectively is, at a minimum, 5.5 percent of the Postal Service's total institutional costs." 39 C.F.R. § 3015.7(c). USPS-FY13-1 shows the Postal Service's total institutional costs in FY 2013 were $33.149 billion, 5.5 percent of which would be approximately $1.823 billion. Competitive products' provided a contribution of $3.899 billion in FY 2013 and thereby satisfied the requirements of 39 U.S.C. § 3633(a)(3) and 39 C.F.R. § 3015.7(c).[80]

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[77] USPS-FY13-NP27, file "SupportGround_FY13.xls", tab "ParcelSelectPRSSummary", comparing cell "E9" with cell "E16" and cell "I9" with cell "I16."

[78] Parcel Return Service Contract 4 Request, Attachment B at 2.

[79] *Id.* Section III also allows the contract to be canceled sooner if cancellation is ordered by the Commission.

[80] *See* USPS-FY13-1, Preface at 7 (contribution calculated by subtracting total competitive attributable costs of $9.762 billion from total competitive product revenue of $13.661 billion).

VIII. CONCLUSION

The Public Representative respectfully submits the foregoing comments for the Commission's consideration.

Respectfully submitted,

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